

D.T.E. 02-51

Petition of Commonwealth Electric Company d/b/a NSTAR Electric for authorization and approval of the issuance of bank term loan agreements not to exceed \$150 million, pursuant to G.L. c. 164, § 14.

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FOR: COMMONWEALTH ELECTRIC COMPANY
d/b/a NSTAR ELECTRIC
Petitioner

I. INTRODUCTION

On September 13, 2002, Commonwealth Electric Company d/b/a NSTAR Electric (“ComElectric” or “Company”), pursuant to G.L. c. 164, § 14, filed a petition with the Department of Telecommunications and Energy (“Department”), requesting approval of a financing plan for the issuance of bank term loans not to exceed \$150,000,000.¹ Pursuant to notice duly issued, a public hearing and an evidentiary hearing were held at the Department’s offices in Boston on October 25, 2002. No petitions for leave to intervene were filed. At the hearing, the Company presented two witnesses in support of its application: Emilie G. O’Neill, director of corporate finance and cash management for the Company, and Philip J. Lembo, assistant treasurer for the Company. The evidentiary record consists of sixteen exhibits and one response to a Department record request. The Company also filed a brief.

II. DESCRIPTION OF THE PROPOSED FINANCING

ComElectric seeks approval to issue indebtedness by the Company, from time to time, on or before December 31, 2004, in the form of one or more bank term loan agreements (each, a “Term Loan”) in an aggregate amount not to exceed \$150,000,000, pursuant to G.L. c. 164, § 14 (Exh. CE-1, at 1). ComElectric’s application is similar to one approved by the Department in Boston Edison Company, D.T.E. 00-62 (2000), where the Department granted Boston Edison Company the authority to issue up to \$500,000,000 of debt securities over the two-year period 2001-2002 (Exh. CE-2, at 6). ComElectric’s application also

¹ Commonwealth Electric last received approval of a financing plan in Commonwealth Electric Company, D.P.U. 92-268 (1993).

proposes a two-year financing period with a maximum amount of \$150,000,000 authorized to be issued (id.). The Company states that it needs the requested two-year flexibility in its financing activities because the timing of its financing needs and the volatility of interest rates make it difficult for the Company to seek timely approval for individual issuances (id.).

The Company's debt will consist of bank term loans with a bank or syndicate of banks (Exh. CE-2, at 7). The Company states that the term loans will have a maturity of greater than one year and will not exceed three years (id.). The Company stated that it was very difficult to secure money for greater than a three-year term under current market conditions (Tr. at 7). The Company states that interest on the term loans would be payable at either a fixed rate (not to exceed ten percent) or an adjustable rate, which will vary with a market index to be designated at the time of issuance, not to exceed ten percent (Exh. CE-2, at 7). The Company states that, in the last five years, three-year fixed rate bank debt has fluctuated from a high of approximately 7.5 percent to a low of approximately 3.5 percent and three-year variable rate bank debt from a high of approximately 7.5 percent to a low of approximately 2.5 percent (id., at 6).

The Company states that the proceeds from the term loans will be used for: (a) the payment at maturity of certain outstanding long-term indebtedness; (b) the payment of capital expenditures relating to extensions, additions, and improvements to the Company's plant and properties, or for the payment of obligations of the Company incurred for such expenditures; (c) the refinancing of the Company's short-term debt balances; and/or (d) general corporate purposes (Exhs. CE-2, at 8; DTE 1-3).

III. STANDARD OF REVIEW

In order for the Department to approve the issuance of stock, bonds, coupon notes, or other types of long-term indebtedness² by an electric or gas company, the Department must determine that the proposed issuance meets two tests. First, the Department must assess whether the proposed issuance is reasonably necessary to accomplish some legitimate purpose in meeting a company's service obligations, pursuant to G.L. c. 164, § 14. Fitchburg Gas & Electric Light Company v. Department of Public Utilities, 395 Mass. 836, 842 (1985) ("Fitchburg II"), citing Fitchburg Gas & Electric Light Company v. Department of Public Utilities, 394 Mass. 671, 678 (1985) ("Fitchburg I"). Second, the Department must determine whether the Company has met the net plant test.³ Colonial Gas Company, D.P.U. 84-96 (1984).

The Supreme Judicial Court has found that, for the purposes of G.L. c. 164, § 14, "reasonably necessary" means "reasonably necessary for the accomplishment of some purpose having to do with the obligations of the company to the public and its ability to carry out those obligations with the greatest possible efficiency." Fitchburg II at 836, citing Lowell Gas Light Company v. Department of Public Utilities, 319 Mass. 46, 52 (1946). In cases where no issue

² "Long-term" refers to periods of more than one year after the date of issuance. G.L. c. 164, § 14.

³ The net plant test is derived from G.L. c. 164, § 16. When the Department approves an issue of new stock, bonds, or other securities by a gas or electric company, if it determines that the fair structural value of the plant and of the land and the fair value of the nuclear fuel, gas inventories, or fossil fuel inventories owned by such company is less than its outstanding stock and debt, it may prescribe such conditions and requirements as it deems best adapted to make good within a reasonable time the impairment of the capital. See G.L. c. 164, § 16.

exists about the reasonableness of management decisions regarding the requested financing, the Department limits its Section 14 review to the facial reasonableness of the purpose to which the proceeds of the proposed issuance will be put. Canal Electric Company, et al.,

D.P.U. 84-152, at 20 (1984); see, e.g., Colonial Gas Company, D.P.U. 90-50, at 6 (1990).

Regarding the net plant test, a company is required to present evidence that its net utility plant (original cost of capitalizable plant, less accumulated depreciation) equals or exceeds its total capitalization (the sum of its long-term debt and its preferred and common stock outstanding) and will continue to do so following the proposed issuance. Colonial Gas Company, D.P.U. 84-96, at 5 (1984).

IV. CAPITAL STRUCTURE OF THE COMPANY

The Company's utility plant, as of June 30, 2002, is \$663,693,649 (Exh. CE-3). The accumulated depreciation against this plant is \$233,439,610 (id.). Thus, as of June 30, 2002, the Company has a net utility plant, excluding accumulated depreciation, of \$430,254,039 (id.). As of June 30, 2002, the Company reported a total capitalization of \$288,387,171, consisting of long-term debt of \$107,097,750, common stock of \$51,099,300, and premium on common stock of \$130,190,121 (id.). The financial statements further illustrate that, as of June 30, 2002, the Company's capital structure consists of 37.13 percent long-term debt, 45.14 percent common stock and 17.73 percent premium on common stock (id.).

V. ANALYSIS AND FINDINGS

The Department finds that the use of the proceeds from the issuance of the term loans for the stated purposes of: a) the payment at maturity of certain outstanding long-term indebtedness; (b) the payment of capital expenditures relating to extensions, additions, and

improvements to the Company's plant and properties, or for the payment of obligations of the Company incurred for such expenditures; (c) the refinancing of the Company's short-term debt balances; and/or (d) general corporate purposes, is reasonably necessary to meet the Company's service obligations and in accordance with G.L. c. 164, § 14. The Department further finds that the Company's proposal to issue the loans on or before December 31, 2004 is appropriate.

In Colonial Gas Company, D.P.U. 84-96, at 8 (1984), the Department required that any company requesting approval to issue new stock, bonds, or other securities to demonstrate that its net utility plant supports the additional amount of financing. Under the net plant test, a company must present evidence showing that its net utility plant (utility plant less accumulated depreciation) is equal to or greater than its total capitalization (the sum of debt, preferred stock and common stock outstanding) (id. at 5).

Initially, the Company had excluded portions of long-term debt that are due within one year from its calculation of the net plant test, asserting that it considered such obligations to be short-term debt (Exh. CE-4; Tr. at 12-13). In response to a request from the Department, the Company recalculated its net plant test to include portions of long-term debt that are due within one year, and, as a result, the Company's net utility plant as of June 30, 2002 is \$430,254,000, while its total capitalization is \$288,387,000, resulting in an excess of net utility plant over outstanding capital of \$141,867,000 (RR-DTE-1).

On brief, the Company argued that its original net plant test calculation is consistent with Department precedent allowing companies to exclude short-term debt (debt payable within one year) from the net plant test (Company Brief at 7-8, citing Southern Union Company,

D.T.E. 01-32, at 10-11 (2001); Southern Union Company, D.T.E. 01-52, at 9-10 (2001)).

However, the Department has previously found that the impending maturity date of a long-term debt issue does not transform the obligation. Nantucket Electric Company,

D.P.U. 91-106/138, at 96 (1991); see also, G.L. c. 164, § 14. Moreover, the Southern Union cases relied on by the Company can be distinguished from the current case. In the Southern Union cases, none of the short-term debt excluded from the net plant test represented portions of a larger long-term debt; the short-term debt excluded from the net plant test in these cases represented a 364-day term loan, i.e., debt that would be paid in full within one year of issuance. D.T.E. 01-32, at 10-11; D.T.E. 01-52, at 9-10.

The Company also notes that generally accepted accounting principles (“GAAP”) would define portions of long-term debt payable within one year as short term debt (Tr. at 13; Company Brief at 7-8). GAAP, while meriting respectful consideration, have but little bearing on the Department’s decision, as it is well settled that financial accounting standards do not automatically dictate Department treatment. See, e.g., Boston Edison Company, D.P.U./D.T.E. 97-95, at 76-77 (1998). This policy extends to the presentation of financial information on the books of the utility, including those for public reporting purposes. GAAP presentation requirements cannot contravene the Department’s statutory duties.

The Company further argued that its original calculation of the net plant test was in accordance with Department precedent because “the Department has not counted maturing debt in the capital structure for purposes of applying the net plant test where the proceeds of a new issuance were to be used, in part, to retire currently outstanding or maturing long-term debt because the Company’s total stock and long-term debt will not exceed the Company’s net plant

after the proposed issuances” (Company Brief at 7, citing Western Massachusetts Electric Company, D.P.U. 91-269, at 7, 9-10 (1992)). In D.P.U. 91-269, however, Western Massachusetts Electric Company proposed, and the Department ordered, that of \$217 million in proceeds from the financing, \$167 million was to be used to pay off existing long-term debt, and \$50 million was to be used to pay off short-term debt. D.P.U. 91-269, at 4-5, 11-13. Hence, D.P.U. 91-269 was, in essence, a re-financing. This is in contrast to the proposal before the Department in this matter, in which only part of the proceeds would be used to pay off existing debt, and the rest would be used to finance capital projects and for general corporate purposes (Exhs. CE-2, at 8; DTE 1-3). Because all of the cases cited by the Company are distinguishable from the current case, the Department rejects the Company’s original net plan test calculation and finds that the second net plant calculation of \$141,867,000 is correct and consistent with Department precedent. See e.g., Boston Edison Company, D.T.E. 00-62 (2000); Colonial Gas Company, D.P.U. 84-96. Unrestricted approval of the total issuance in this case would result in outstanding debt exceeding net utility plant by \$8,133,000 (\$150,000,000 - \$141,867,000) (RR-DTE-1). The Company’s capital structure currently is not sufficient to support the size of the proposed issuance. Rather, the Company’s current capital structure is sufficient to support the proposed issuance of \$141,867,000 in debt in 2002.

In similar cases, the Department has approved financings with certain conditions imposed on a company until any net plant impairment had been remedied. See e.g., Boston Edison Company, D.T.E. 00-62, at 10-11; East Northfield Water Company, D.P.U./D.T.E. 97-36, at 6-7 (1997); Colonial Gas Company, D.P.U. 95-76, at 7-8 (1995).

Having found the proposed financing is reasonably necessary to meet the Company's service obligations and in accordance with G.L. c. 164, § 14, the Department will approve the Company's plan with certain conditions to ensure that the value of the Company's existing capital stock will not be impaired. Pursuant to G.L. c. 164, § 16, as an appropriate safeguard to its financial integrity, the Company shall issue no more than \$141,867,000 in debt through March 3, 2003. After March 3, 2003, the Company may issue up to \$8,133,000 in additional debt, provided that it makes a supplemental compliance filing in this docket showing that it can meet the net plant test at that time.

Issues concerning the prudence of the Company's capital financing have not been raised in this proceeding, and the Department's decision in this case does not represent a determination that any project is economically beneficial to the Company or its customers. The Department's determination in this Order is not in any way to be construed as a ruling relative to the appropriate ratemaking treatment to be accorded any costs associated with the proposed financing.

VI. ORDER

Accordingly, after due notice, hearing, and consideration, the Department

VOTES: That the issuance, from time to time on or prior to December 31, 2004, by Commonwealth Electric Company d/b/a/ NSTAR Electric, of term bank loans, in an amount not to exceed \$150,000,000, is reasonably necessary for the purposes for which such issuance has been authorized; and it is

ORDERED: That the issuance, from time to time on or prior to December 31, 2004, by Commonwealth Electric Company d/b/a/ NSTAR Electric, of term bank loans, in an

amount not to exceed \$150,000,000, is reasonably necessary for the purposes for which such issuance has been authorized; and it is

FURTHER ORDERED: That such authorized term bank loans issued by Commonwealth Electric Company shall carry a fixed interest rate not to exceed an effective rate of ten percent per annum, or an adjustable rate to vary with a market index designated at the time of issue or in accordance with a market auction mechanism, but which will not exceed ten percent per annum; and it is

FURTHER ORDERED: That Commonwealth Electric Company shall not issue more than \$141,867,000 of this long-term debt on or prior to March 3, 2003; and it is

FURTHER ORDERED: That the net proceeds from such term bank loans shall be used for the purposes as set forth herein; and it is

FURTHER ORDERED: That the Secretary of the Department shall within three days of the issuance of this Order cause a certified copy of it to be filed with the Secretary of the Commonwealth.

By Order of the Department,

Paul B. Vasington, Chairman

James Connelly, Commissioner

W. Robert Keating, Commissioner

Eugene J. Sullivan, Jr., Commissioner

Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).